No. 85-533

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In The

Supreme Court of the United States

October Term, 1985

SILENT HOIST AND CRANE CO., INC.,

Petitioner,

vs.

DIRECTOR, DIVISION OF TAXATION,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF NEW JERSEY

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QUESTIONS PRESENTED

1. Whether the presence of unrelated tangible assets within the taxing state may satisfy the nexus requirements of the Due Process and Interstate Commerce Clauses for the tax apportionment of the income from the investment securities of a nondomiciliary corporation on the grounds that the securities contribute to the general capital assets of the corporation.

2. Whether, as the New Jersey Supreme Court has ruled, *Container Corporation of America v. Franchise Tax Board* overruled *F.W. Woolworth Co. v. Taxation & Rev. Dept.* and *Asarco, Inc. v. Idaho State Tax Comm'n.* so as to restore the corporate purpose doctrine, under which the contribution of activities and assets outside the taxing state to a nondomiciliary corporation's overall purpose of profit making will sustain the imposition of an apportioned income tax without any further nexus of these assets and activities to the taxing state.

3. Whether the Due Process and Interstate Commerce Clause standards that will sustain the imposition of a tax on the apportioned income of a nondomiciliary corporation in light of *Container Corporation of America v. Franchise Tax Board*, are now identical to the jurisdictional standards that will sustain the imposition of liability for remittance of a state sales and use tax.

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No.

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DIRECTOR, DIVISION OF TAXATION,

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PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF NEW JERSEY

Silent Hoist and Crane Co., Inc., petitions for a writ of certiorari to review the judgment of the New Jersey Supreme Court in this case.

OPINIONS BELOW

The opinion of the New Jersey Supreme Court (App. *infra*, 1a) is reported at 100 N.J. 1. The decision of the New Jersey Appellate Division (App. *infra*, 47a) is reported at 6 N.J. Tax 348. The decision of the Tax Court of New Jersey (App. *infra*, 30a) is reported at 5 N.J. Tax 242.

JURISDICTION

The judgment of the New Jersey Supreme Court was entered on June 26, 1985. The jurisdiction of this Court is invoked under 28 U.S.C. § 1257(3).

STATUTES INVOLVED

Relevant provisions of the New Jersey Corporation Business Tax Act, *N.J. Stat. Ann.* 54:10A-1, *et seq.* are reprinted at App., *infra*, 49a.

STATEMENT

1. The Supreme Court of New Jersey has held that petitioner's corporation is a unitary business and hence that its sales and investment income are subject to the New Jersey Corporation Business Tax Act, *N.J. Stat. Ann.* 54:10A-1 *et. seq.* (West 1960). The issue presented by this case is the proper test to be applied by a court in determining whether a corporation is unitary for tax purposes. Before turning to the facts of this case, we set forth a brief description of corporate business taxes in New Jersey and the statutory and regulatory scheme for their collection.

a. As a general rule, "a State may not tax value earned outside its borders." *Asarco, Inc. v. Idaho State Tax Comm'n*, 458 U.S. 307, 315 (1982). Both Due Process and the Commerce Clauses of the U.S. Constitution bar states from taxing income arising out of interstate activities without a "minimal connection" or nexus between those interstate activities and the taxing state and a "rational relationship between the income attributed to the State and the intrastate value of the enterprise." *Exxon Corp. v. Wisconsin Dept. of Revenue*, 447 U.S. 209, 219-20 (1980); *Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425, 436-37 (1980).

This connection may be established by a finding that the taxpayer conducts a unitary business. *See generally* Keesling & Warren, "The Unitary Concept in the Allocation of Income," 12 Hastings L.J. 42 at 43-49 (1960). The finding of a unitary business is a necessary prerequisite to the ultimate conclusion that the taxpayer's in-state activities contribute in some material way to its out-of-state earnings. The necessity of such a finding is established by the principle that a state may not levy a tax on a corporation unless it has provided a service for which it can ask a return. *Wisconsin v. J.C. Penney Co.*, 311 U.S. 435, 444 (1940). In short, "the linchpin of apportionability in the field of state taxation is the unitary business principle." *Mobil Oil, supra* at 439.

b. New Jersey's answer to the constitutional problems raised by multi-state taxation is the New Jersey Corporation Business Tax Act, *N.J. Stat. Ann.* 54:10A-1 *et. seq.* (West 1960). This act applies an "allocation formula" to the net worth and net income tax bases of a corporation so that only those portions that may be fairly attributed to New Jersey activities are subject to New Jersey tax. *See N.J. Stat. Ann.* 54:10A-6. The statute calls for the consideration of three factors, payroll, property and receipts. The multi-state total of the taxpayer's payroll, property and receipts constitutes the denominator of a fraction while the numerator is composed of the taxpayer's New Jersey payroll, property and receipts. *N.J. Stat. Ann.* 54:10A-6(B). The average is then taken of these three fractions. The resultant, known as the "allocation factor" is applied to the taxpayer's net worth and net income to reach a determination as to the percentage of worth and income taxable by New Jersey. [For a more detailed discussion of the mechanics of this statute *see Metromedia, Inc. v. Director, Division of Taxation*, 97 N.J. 313 (1984).]

The Director, Division of Taxation is given the authority to adjust the allocation factor to more accurately reflect the extent of the taxpayer's activities within the state. Under *N.J. Stat. Ann.*

54:10A-8 he may specifically: (a) exclude any of the factors; (b) include any other factor; (c) exclude any assets in calculating net worth; (d) exclude any assets in calculating an allocation percentage; or (e) apply any other method to "effect a fair and proper allocation of the entire net income and the entire net worth reasonably attributable to the state."

2. Silent Hoist and Crane Co., Inc. is a New York corporation which engineers and fabricates special purpose, heavy duty materials handling equipment. It has both its principal place of business and its manufacturing plant in Brooklyn, New York. Silent Hoist is a privately held corporation. Its president and chief operating officer is Eric Wunsch. The corporation conducts business by sending its sales representatives, who are themselves engineers, to potential customers to survey their needs. This contact is normally initiated by the customers themselves. This would be followed by a design conference either in Brooklyn, in New Jersey or at locations where a similar piece of machinery could be found.

The manufacture of the equipment would take place usually in Brooklyn though occasionally in Connecticut and the machines would then be delivered to New Jersey. If problems arose the company's representatives would show the customer how to deal with them and would, on occasion, arrange for machine parts to be shipped back to the plant for repair.

During the period in question, the sole physical links that Silent Hoist had with New Jersey were two parcels of industrially zoned land owned by the taxpayer in Clifton and Bloomfield, New Jersey. The deposition testimony of Silent Hoist's president indicated that the purpose of the real estate holdings was diversification, that it had no relationship to the manufacturing business. Although the Tax Court made no specific finding on this, the Supreme Court stated that Silent Hoist "originally intended to move its plant to Clifton but abandoned the idea"

(App., *infra*, 15a). This statement finds no support in the record. Whatever idea later occurred to Silent Hoist, there was no original intent to move any of its operations to New Jersey.

The buildings on these lots were rented to industrial tenants on the basis of net leases. None of these tenants were related to Silent Hoist's manufacturing operations. This New Jersey real estate venture operated at a net loss. Accordingly, Silent Hoist had reported losses totaling over $300,000 on the income statements included with its tax returns for the years in question. The corporation utilized the services of professional real estate brokers to rent the properties and provide guidance in their management. It was because of these New Jersey properties that Silent Hoist obtained a certificate to do business in this state.

Silent Hoist also maintained a securities investment portfolio which was not related in any way to the manufacturing or real estate operations. The Tax Court found that all securities were solely for investment purposes and were all held in New York by a professional broker who oversaw the day to day operations. A majority of the portfolio consisted of common and preferred stocks in companies which were not controlled by Silent Hoist and which were not in precisely the same line of business as that corporation. The Tax Court found that Silent Hoist did not advertise in New Jersey magazines or newspapers, and did not have a telephone listing in New Jersey. In addition, Silent Hoist did not have any offices or other facilities in New Jersey, had no employees or payroll in New Jersey, made no installations or deliveries in New Jersey and directed no marketing efforts toward New Jersey (App. *infra*, 40a).

Silent Hoist's total sales figures in New Jersey were $436,566 in 1971, $986,862 in 1972, $988,740 in 1973 and $706,410 in 1974. However, the Tax Court found that, in light of the sale prices for each machine which ranged from $50,000 to $200,000 these sales were not of any great magnitude (App., *infra*, 41a).

When Silent Hoist filed its CBT returns in New Jersey for the period in question, it reported only its income and expenses related to the New Jersey real estate operations in computing the net income tax portion of its returns. It included an attachment explaining that this adjustment was an attempt to fairly comply with the New Jersey Corporate Business Tax Act. The Director, Division of Taxation, rejected this adjustment and assessed Silent Hoist for deficiencies in the amounts of $9,618.51 for 1971, $18,832.82 for 1972, $19,800.91 for 1973 and $1,089.22 for 1974 not including interest. Silent Hoist then submitted a formal petition for adjustment pursuant to *N.J. Stat. Ann.* 54:10A8. The Director denied the petitions and Silent Hoist appealed to the Tax Court of New Jersey.

Upon review, the Tax Court found that Silent Hoist's real estate holdings in New Jersey "represented taxpayer's sole tangible connection with this state" (App., *infra*, 32a). It applied the three indicia of a unitary business set forth in *Asarco, Inc. v. Idaho, supra*, functional integration, centralization of management and economies of scale. Utilizing this test, the Tax Court found that Silent Hoist was not a unitary business but that it was actually three distinct operations; manufacturing, real estate and securities investments. It found no relationship between these three elements. It therefore held that the only portions of entire net worth and entire net income includable in the New Jersey returns were the real estate holdings. The court also rejected the arguments of the Director that Silent Hoist could be described as having centralized management calling it instead centralized ownership (App., *infra*, 44a). On April 4, 1984 the Appellate Division affirmed the Tax Court per curiam, without opinion.

3. The New Jersey Supreme Court reversed holding that Silent Hoist was a unitary business as this court has defined that term (App., *infra*, 1a). The court found that, contrary to the factual findings of the Tax Court, Silent Hoist's President "exercised

effective control over all areas of the company's operations" (App., *infra*, 16a). It also differed from the findings of the Tax Court by holding that Silent Hoist bought the New Jersey real estate with the intention of moving its manufacturing operations there (App., *infra*, 21a).

The essential difference between the Tax Court holding and that of the New Jersey Supreme Court, however, was in the legal principles to be applied. In the time between these two decisions this Court handed down its opinion in *Container Corporation of America v. Franchise Tax Board*, 463 U.S. 159 (1983). The New Jersey Supreme Court seized upon this case and held that it supplanted both *F.W. Woolworth Co. v. Taxation and Revenue Dep't. of New Mexico*, 458 U.S. 354 (1982) and *Asarco*, confining both those cases to their specific facts (App., *infra*, 28a). As authority for this far reaching conclusion the New Jersey Supreme Court relied on two student written law review notes. Note, "The Supreme Court 1982 Term," 97 *Harv. L. Rev.* 70 (1983) and Note, "State Taxation of Multinationals and the Unitary Business Concept: A Contemporary View." 10 *Brooklyn J. of Int'l Law* 115 (1984).

As a result, the three part standard of *Mobil Oil* was rejected by the New Jersey Supreme Court. It was replaced by the amorphous test of whether there have been "unquantifiable transfer of value . . . among the components of a single enterprise" (App., *infra*, 19a quoting *Container Corp., supra* at 178).

With this as the only test, the court had no trouble finding that Silent Hoist was a unitary business. It was able to tie in the real estate to the manufacturing business by positing that the land was "presumably" purchased with the use of general corporate funds and that expenses for the years the property was not rented were paid from that same sources (App., *infra*, 21a, 22a). The

securities portfolio was likewise tied in with the rest of the corporation because it "was capable of being pledged, liquidated or converted to other uses of the company's sales or real estate operations" (App., *infra*, 23a).

Following this conclusion, the New Jersey Supreme Court remanded this case to the Appellate Division to determine whether the assessment was "out of all appropriate proportion" to the taxpayer's New Jersey activities [App., *infra*, 29a citing *Hans Rees Sons, Inc. v. North Carolina ex rel. Maxwell*, 283 U.S. 123 (1931)].

REASONS FOR GRANTING THE WRIT

At the outset, it is important to note that the decision of the New Jersey Supreme Court is ripe for review by this Court. 28 U.S.C. § 1257(3) gives this Court statutory authority to review the final judgment of any state Supreme Court. Although the New Jersey Supreme Court remanded this case for further consideration on the issue of proportionality, such a remand is not fatal to a review by certiorari.

It is a well established exception to the general rule that when the federal issues as determined by the highest state court will survive any possible outcome of future state court proceedings certiorari will lie. *Cox Broadcasting Corp. v. Cohn*, 420 U.S. 469, 480 (1975). This is in keeping with the earlier holding of this Court warning against a too mechanical application of this rule. *Radio Station WOW, Inc. v. Johnson*, 326 U.S. 120 (1945).

The instant case falls well within this exception to the final judgment rule. No matter what adjustments are made on remand, the essential holding of the New Jersey Supreme Court will not change. The values of the securities portfolio and the manufacturing operations will still be included in ascertaining Silent Hoist's New Jersey income even if not in precisely the same

amounts. More importantly, the holding of the New Jersey Supreme Court effectively overruling this Court's decisions in *Woolworth* and *Asarco* will still stand pending review by this Court.

The decision below should be reversed because it is flatly inconsistent with the settled decisions of this Court. The confusion caused by this decision disrupts the orderly administration of the assessment of corporation business taxes in New Jersey and in any other state with a similar holding by its highest court. Either the decision below misinterprets the import of this Court's opinion in *Container Corp. supra*, or, if it does not so misinterpret, the issues of far reaching importance left undecided in that case must be faced. In either event, this Court should grant review.

1. The Court below could not reconcile the decision of this Court in *Container Corp.* with those in *Woolworth* and *Asarco*. It held that "(t)he *Container* decision 'implies that the Court's holdings in *Woolworth* and *Asarco* can be confined to their specific facts.' Note, 'State Taxation of Multinationals and the Unitary Business Concept: A Contemporary View', 10 *Brooklyn J. of Int'l Law*, 115, 145 (1984)" (App., *infra*, 28a).

The confusion of the court below arises from the language of this Court in *Container Corp.* that "(t)he prerequisite to a constitutionally acceptable finding of unitary business is a flow of value." 463 U.S. 178. The New Jersey Supreme Court suggests that this is a new standard, less stringent and far broader than the three part test enunicated by this Court in *Mobil Oil* and reemphasized in *Woolworth* and *Asarco*, that a unitary business is one which results from "functional integration, centralization of management and economies of scale." *Mobil Oil Corp., supra*, 445 U.S. at 438. It was by applying this three part test that the Tax Court made the factual finding that Silent Hoist was not a unitary business but was comprised of three distinct operations,

manufacturing, real estate and securities investments (App., *infra*, 46a). Under these same facts, the New Jersey Supreme Court reached the opposite conclusion. The difference is the test applied.

In fact, in holding that *Container Corp.* impliedly overruled both *Woolworth* and *Asarco* the New Jersey Supreme Court is doing more than misinterpreting one case, it is rejecting an entire line of authority.

The holding of the court below is incorrect for several reasons. First, it is clear that the aforementioned three decisions of this Court are fully consistent with each other. In *Container Corp.* this Court recognized the long standing principle that

> the out-of-State activities of the purported 'unitary business' be related in some concrete way to the in-State activities. The functional meaning of this requirement is that there be some sharing or exchange of value not capable of precise identification or measurement—beyond the mere flow of funds arising out of a passive investment or a distinct business operation—which renders formula apportionment a reasonable method of taxation.

463 U.S. at 166.

The New Jersey Supreme Court ignored the clear mandate of this holding and instead focused on the separate language of the *Container* decision requiring the existence—of a "flow of value." 463 U.S. at 178. When the "flow of value" language is taken in context, its consistency with the prior decisions of this Court is evident. The "flow of value" language appears in a discussion of the suggestion by the appellant to establish a so called "bright-line rule" requiring the finding of a "substantial

flow of goods" before the existence of a unitary business could be established. A flow of goods would seem to suggest the presence of that degree of "mutual interdependence" which is a prerequisite to a finding of unitariness. 463 U.S. at 179. Of course, a flow of goods. does not, in and of itself, establish the existence of a unitary business. It is only when the flow of goods is the product of functional integration, centralized management and economies of scale that the finding of unitariness is justified. *Container Corp. supra*, 463 U.S. at 179. This was the context in which this Court used the language of a "flow of value."

Therefore, it can more accurately be said that the flow of goods is only an example of "the many subtle and largely unquantifiable" ways in which one division of a corporation may be tied in to another through functional integration, centralization of management and economies of scale. 463 U.S. at 164-65. It is not the only way. Thus it is only in the context of the rejected flow of goods test that one may legitimately say that the flow of value standard is a broader and less stringent standard because flow of goods is really nothing more than a subset of flow of value. Both of these standards must be measured against the mutual interdependence evidenced by functional integration, centralization of management and economies of scale as they are both a product of that interdependence.

The importance of the New Jersey Supreme Court's confusion over the test to be applied is clearly understood when one considers the constitutional underpinnings of this line of decisions. It is important not to lose sight of the fact that a State may not tax values earned outside its own borders. *See, Connecticut General Life Ins. Co. v. Johnson*, 303 U.S. 77, 80-81 (1938). The same holds true under both Due Process and Commerce Clause challenges. There must be a minimal connection or nexus between the interstate activities and the taxing State, and a rationale relationship between the income attributed to the State and the

intrastate values of the enterprise." *Container Corp., supra*, 463 U.S. at 165-66.

This is where the finding of a unitary business comes into play. If the corporation is unitary, the State need not establish an individual nexus to each of the activities as long as the activities of the corporation itself are related to each other in some concrete way. Thus if too liberal a standard of unitariness is adopted the constitutional ramifications are obvious. In the absence of a more stringent test to establish the existence of a unitary business, the minimal nexus necessary to satisfy the dictates of the Constitution may not be present.

It is in this context that the flow of value standard taken as the sole test of unitariness runs afoul of the decisions of this Court interpreting the Commerce Clause and the requirements of Due Process. The result in this very case shows the danger of relying solely on so precarious a standard.

The sole tangible connection of Silent Hoist to the State of New Jersey is the presence of two pieces of real estate which are themselves loss producing. Utilizing the flow of value standard, the New Jersey Supreme Court held that the real estate was tied to the security portfolio because "Silent Hoist's investment capital was capable of being pledged, liquidated or converted to other uses of the company's sales or real estate operations" (App., *infra*, 23a). It is hard to imagine a more tenuous connection. Under such a standard, any corporation that held even a single share of stock in a wholly unrelated business would be classified as unitary because it could theoretically use that stock to finance its operations elsewhere.

Under the same analysis, the manufacturing and sales division of Silent Hoist was held to be tied to the New Jersey real estate as the purchase price for and expenses of the property were

"presumably" paid out of general corporate funds (App., *infra*, 21a, 22a). Under this analysis virtually any corporation would be subject to a finding of unitariness on the basis of its accounting practices. However, the relevance of accounting practice in determining the status of a corporation has been specifically rejected by this Court. *See Butler Bros. v. McColgan*, 315 U.S. 501, 506-08 (1942). The holding by the court below is an unwarranted return to that rejected standard.

The New Jersey Supreme Court also attempts to return to the now abandoned corporate purpose doctrine. The corporate purpose doctrine is best described as an expansive definition of the term "unitary business" that would be satisfied merely by evidence that operationally disassociated activities contributed to the corporation's overall profitability. This theory focuses on a corporation's ultimate purpose of profit making, as being the final "business" of the company. Given this all inclusive starting point, a corporation's diversified operations, and even its intangible securities investments, form parts of a single enterprise with the unified goals of achieving financial strength.

The corporate purpose doctrine is derived from this Court's decision in *Flint v. Stone Tracy Co.*, 220 U.S. 107 (1910) a federal excise tax case which stands for the proposition that any corporate asset contributes to a corporation's "unified" purpose of profit making since:

> . . . it may give credit which will result in more economical business methods; it may give a standing which shall facilitate purchases; it may enable the corporation to enlarge the field of its activities and in many ways give it business standing and prestige.

220 U.S. at 166.

This Court has subsequently rejected that doctrine in its entirety. In *Asarco, supra*, this Court noticed that an anaylsis such as the one performed by the court below leads to a self-fulfilling result, a result that is unacceptable under the Interstate Commerce and Due Process Clauses:

> Idaho's (taxing state) proposal is that corporate purpose should define unitary business . . .this definition of unitary business would destroy the concept. The business of a corporation requires that it earn money to continue operation and to provide return on its invested capital. Consequently all of its operations, including any investment made, in some sense can be said to be for "purposes related to or contributing to the (corporation's) business." When pressed to its logical limit, this conception of the "unitary business" limitation becomes no limitation at all. When less ambitious interpretations are employed, the result is simply arbitrary.

458 U.S. at 326.

In holding that the ultimate pooling of profits in a single bank account, as was the case here, was irrelevant to the proper application of the unitary business principle, this Court stated in *Woolworth* that:

> . . .the New Mexico Supreme Court also thought it significant that *Woolworth* commingled its dividends with its general funds and had used them for general corporate operating purposes . . .This analysis likewise subverts the unitary business limitation. *All* dividend income—irrespective of whether it is generated by a "discrete business

> enterprise," would become part of a unitary business if the test were whether the corporation commingled dividends from other corporations, whether subsidiaries or not.

458 U.S. at 363.

The Court elaborated on the syllogistic reasoning inherent in the corporate purpose doctrine, and specifically rejected the *Flint* decision.

> This reliance on the *Flint* case was error. *Flint* upheld a federal excise tax levied on corporate income. The States, of course, are subject to limitations on their taxation powers that do not apply to the Federal Government. As relevant here, "the income attributed to a State for tax purposes" must be rationally related to values connected with the State. (citations) The state court's reasoning would trivialize this due process limitation by holding it satisfied if the income in question "adds to the riches of the corporation . . ." (citation). Income, from whatever source, always is a "business advantage" to a corporation. Our cases demand more. In particular, they specify that the property inquiry looks to the "underlying unity or diversity of business enterprise," . . .not to whether the nondomiciliary parent derived some economic benefit—as it virtually always will—from its ownership of stock in another corporation.

458 U.S. at 363-364.

Nor may it be argued that this Court's decision in *Container Corp.* harkened a return to the corporate purpose doctrine.

Rather than adopting a "less stringent" test, the *Container Corp.* decision reaffirmed the Court's recent *Mobil, Exxon, Woolworth* and *Asarco* opinions as illustrating the different results obtainable under varying factual circumstances. In *Container Corp.* the Court also makes clear, that in ascertaining whether there has been a "flow of value" among the segments of corporation's operations, that will support a unitary business finding, the relevant inquiry is not whether any one division of the corporation's business has contributed to the corporation's overall income. Rather, the inquiry is whether any income contribution has been achieved through "functional integration, centralization of management, and economics of scale." *Container Corp.* 463 U.S. at 179. The Court further noted that unitary status requires a "concrete relationship between the facets of a corporation's operations, going "beyond the mere flow of funds arising out of a passive investment or a distinct business operation." *Id.*, 463 U.S. at 166.

As discussed in more detail elsewhere in this petition, the court below made numerous findings of fact and conclusions of law which could be relevant only under this rejected standard. The court's finding that the securities portfolio could have been used to finance manufacturing and that the money for the New Jersey property "presumably" came from general corporate funds are irrelevant outside the confines of the corporate purpose doctrine. In addition, the court's emphasis on the purported corporate intent to transfer its manufacturing operations to one of the New Jersey properties, an intent never even established by the trial court, could not have any relevance other than under the corporate purpose doctrine. The New Jersey Supreme Court's attempt to resurrect that standard must be reviewed.

Nor is the fact that Silent Hoist may have, in some instances, remitted taxes under New Jersey's Sales and Use Tax Act, *N.J. Stat. Ann.* 54:32B-1 (West 1960) relevant to a finding of

apportionability. In the first place, Silent Hoist never conceded, nor was it ever adjudged that this tax was properly payable by Silent Hoist. Secondly, a sales tax is assessed under far different constitutional standards than an income tax. A sales tax is not a direct charge on interstate commerce. It is an assessment on the purchaser of goods that will be used within the taxing state. Thus a sales tax may be proper under factual circumstances which would not support the apportionment by a state of tax on a corporation's income. As this Court stated in *Norton v. Dept. of Revenue*, 340 U.S. 534 (1951):

> Where a corporation chooses to stay at home in all respects except to send abroad advertising or drummers to solicit orders which are sent directly to the home office for acceptance, filling, and delivery back to the buyer, it is obvious that the state of the buyer has not local grip of the seller. Unless some local incident occurs sufficient to bring the transaction within its taxing power, the vendor is not taxable. (citations) Of course, a state imposing a sales or use tax can more easily meet this burden, because the impact of those taxes is on the local buyer or user. *Cases involving them are not controlling here*, for this tax falls on the vendor.

340 U.S. at 537 (emphasis added).

See also, National Geographic Society v. California Bd. of Equalization, 430 U.S. 551 (1977). Thus, even if the manufacturing business of Silent Hoist was present in New Jersey for purposes of the applicability of the state sales tax, it was not so present for the purposes of an income tax. Clearly, the holding of the New Jersey Supreme Court is inconsistent with the decisions of this Court and tests the outer limits of constitutional doctrine.

In short, the New Jersey Supreme Court has misinterpreted the holding of this Court in *Container Corp.* In fact, the New Jersey Supreme Court erred in applying *Container Corp.* to the facts before it in the first place. The analysis in *Container Corp.* is inextricably bound up with the peculiar facts of that case. It involved an American parent company with foreign subsidiaries. A large part of the analysis dealt with the constitutionality of worldwide combined reporting and with an explanation of the import of this Court's decision in *Japan Lines Ltd. v. County of Los Angeles*, 441 U.S. 434 (1979). In fact, this Court specifically stated in *Container Corp.* that the constitutional scrutiny involved was different under the foreign Commerce Clause. 463 U.S. at 115. Thus, contrary to the holding of the court below that in light of *Container Corp.*, both *Woolworth* and *Asarco* have been confined to their facts, in the context of this case it is *Container Corp.* which must be confined to its facts.

The decision of the New Jersey Supreme Court is not only flatly inconsistent with the previous decisions of this Court, it is also contrary to the intent of Congress.

In reaction to this Court's decision in *Northwestern States Portland Cement Co. v. Minnesota,* 358 U.S. 450 (1959) Congress enacted 15 U.S.C. § 381 (West 1976). This statute provides in pertinent part:

> (a) No State, or political subdivision thereof, shall have power to impose, for any taxable year ending after September 14, 1959, a net income tax on the income derived within such State by any person from interstate commerce if the only business activities within such State by or on behalf of such person during such taxable year are either, or both, of the following:

(1) the solicitation of orders by such person, or his representative, in such State for sales of tangible personal property, which orders are sent outside the State for approval or rejection, and, if approved, are filled by shipment or delivery from a point outside the State; and

(2) the solicitation of orders by such person, or his representative, in such State in the name of or for the benefit of a prospective customer of such person, if orders by such customer to such person to enable such customer to fill orders resulting from such solicitation are orders described in paragraph (1).

(b) For purposes of subsection (a) of this section, a person shall not be considered to have engaged in business activities within a State during any taxable year merely by reason of sales in such State, or the solicitation of orders for sales in such State, of tangible personal property on behalf of such person by one or more independent contractors, or by reason of the maintenance, of an office in such State by one or more independent contractors whose activities on behalf of such person in such State consist solely of making sales, or soliciting orders for sales, of tangible personal property.

(c) For purposes of this section—

(1) the term "independent contractor" means a commission agent, broker, or other independent contractor who is engaged in selling, or soliciting orders for the sale of,

> tangible personal property for more than one principal and who holds himself out as such in the regular course of his business activities; and
>
> (2) the term "representative" does not include an independent contractor.

This statute is applicable to the instant situation as the Corporation Business Tax Act is measured, in part, by net income. *See* 15 U.S.C. § 383. It is also relevant to the within facts because Silent Hoist has engaged in the activities which Congress expressly declared are insufficient to establish a nexus.

Yet under the flow of value standard approved by the court below, these same facts, standing alone, are sufficient to constitute a nexus. A corporation which conducts its business in the manner contemplated by the statute would, of course, receive money from its sales. If this money is then used to help finance another entity's in-state activities or holding, the nexus is established. This is not what Congress intended by the enactment of this statute. It was just such a tenuous link to in-state sales that Congress flatly rejected. The New Jersey Supreme Court may not overrule both this Court and Congress in one fell swoop. Its decision threatens to increase the uncertainty of doing business by multi-state corporations who will not know by what standard they will be judged.

As a practical matter, a corporation engaged in multi-state activities, as so many are, will not know which way to turn to avoid unfair apportionment. Limiting itself to the type of business envisioned in 15 U.S.C. § 381 will not help as the New Jersey Supreme Court has effectiveiy undermined the security promised by the congressional enactment.

Nor would an atternpt to abide by the New Jersey Supreme Court's amorphous "flow of value" standard be successful for that is simply no standard at all. The court below recognized this itself when it stated "the unitary business in the end may simply be something that the Court knows when it sees it" [App., *infra*, 28a quoting W. Hellerstein, "State Income Taxation of Multijurisdictional Corporations, Part II: Reflection on *Asarco* and *Woolworth*." 81 *Mich L. Rev*, 157, 178-179 (1982)]. This standard, if it truly can be called one, has been widely criticized when applied to the subject of its origin, the obscenity doctrine. It should have no application at all in an area such as this, untouched by First Amendment concerns.

Finally, it should fairly be noted that the New Jersey Supreme Court is not alone in its confusion over the meaning and import of *Container Corp.* The decisions of the highest courts in other states are equally inconsistent with each other and with the decisions of this Court. Compare *Russell Stovers Candies, Inc. v. Dept. of Revenue*, 665 P. 2d 198 (Sup. Ct. Mont. 1983), *app. dism'd*, ____ U.S. ____, 104 S. Ct. 475, *reh. den.* ____ U.S. ____, 104 S. Ct. 1018 (1983) with *Commissioner of Revenue v. Associated Dry Goods, Inc.*, 347 N.W. 2d 361 (Sup. Ct. Minn. 1984) *cert. den.* ____ U.S. ____, 83 L. Ed. 2d 66 (1984).

Scholarly articles too have been unable to agree on the correct interpretation of the *Container Corp.* decision. Compare White Nack, "State Tax Litigation after the Container Decision," 1983 Tax Notes 771 with Hreha & Seago, "Domestic and Foreign Aspects of the Container Decision," 2 J. of St. Tax'n 101 (1983) and Peters, "Supreme Ct. in Container Upholds State's Broad Power Under Unitary Taxation Method," 59 J. of Tax'n 300 (1983). Accordingly, due to the inconsistent interpretations of *Container Corp.* clarification of that decision and of the appropriate test for unitariness is required for the benefit of states and business alike.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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September 24, 1985

APPENDIX A — OPINION OF SUPREME COURT OF NEW JERSEY

SUPREME COURT OF NEW JERSEY

SILENT HOIST & CRANE CO., INC., A CORPORATION OF THE STATE OF NEW YORK,

PLAINTIFF-RESPONDENT,

v.

DIRECTOR, DIVISION OF TAXATION,

DEFENDANT-APPELLANT.

Argued January 8, 1985 -- Decided June 26, 1985.

O'HERN, J.

This appeal concerns the validity of a franchise tax assessment against a New York corporation doing business in New Jersey. The taxpayer challenged the inclusion, as part of the value of its franchise, of allocated portions of (1) income derived from investment of corporate funds, and (2) certain machinery sales in New Jersey and elsewhere. We agree with the Director of the Division of Taxation that the taxpayer conducts its business as a "unitary business" and consequently we hold that the assessment reflects the value of the franchise fairly apportioned to New Jersey and thus does not offend the Due Process or Commerce Clauses of the United States Constitution. Accordingly, we reverse the judgment below that disallows the assessment.

Appendix A

I.

State Taxation of Interstate Business

For over sixty years it has been a settled principle of federalism that a state tax on corporations doing business within a state is not limited to transactions within that state so long as the tax is fairly apportioned. *Underwood Typewriter Co. v. Chamberlain,* 254 *U.S.* 113, 41 *S.Ct.* 45, 65 *L.Ed.* 165 (1920). That case, like this one, involved the manufacture of products in one state and their sale in another. Connecticut used a single-factor formula to allocate Underwood's income from typewriter sales based on property located in Connecticut. Underwood contended that the formula taxes "income arising from business conducted beyond the boundaries of the state," in violation of the Due Process Clause. *Id.* at 120, 41 *S.Ct.* at 46, 65 *L.Ed.* at 169. Justice Brandeis rejected the claim, stating that Connecticut "adopted a method of apportionment which, for all that appears in this record, reached, and was meant to reach, only the profits earned within the state," *id.* at 121, 41 *S.Ct.* at 47, 65 *L.Ed.* at 169, and held that the taxpayer had failed to carry its burden of proving that "the method of apportionment adopted by the state was inherently arbitrary or that its application to this corporation produced an unreasonable result." *Id.* at 121, 41 *S.Ct.* at 47, 65 *L.Ed.* at 169-70 (footnotes omitted).

This underlying principle has continually informed the Supreme Court's treatment of state taxation of businesses that gain income from more than one state. A state is not constitutionally limited to taxing only that slice of an interstate enterprise operating physically within the state. *See, e.g., Hans Rees' Sons, Inc. v. North Carolina et rel. Maxwell,* 283 *U.S.* 123, 51 *S.Ct.* 385, 75 *L.Ed.* 879 *S.Ct.* 385 (1931); *Bass, Ratcliff &*

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Gretton, Ltd. v. State Tax Comm'n, 266 *U.S.* 271, 45 *S.Ct.* 82, 69 *L.Ed.* 282 (1924); *Underwood Typewriter Co., supra,* 254 *U.S.* 113, 41 *S.Ct.* 45, 65 *L.Ed.* 165. In a long series of decisions the Court has also discarded the formalisms that had obscured its analysis. Thus, in *Northwestern States Portland Cement Co. v. Minnesota,* 358 *U.S.* 450, 79 *S.Ct.* 357, 3 *L.Ed.*2d 421 (1959), the Court held that the Constitution did not bar, as a direct tax on interstate commerce, states from taxing, on an apportioned basis, the net income of foreign corporations that sold their products solely in interstate commerce. *Id.* at 461-62, 79 *S.Ct.* at 363-364, 3 *L.Ed.*2d at 429-30. Finally, in *Complete Auto Transit, Inc. v. Brady,* 430 *U.S.* 274, 97 *S.Ct.* 1076, 51 *L.Ed.*2d 326 (1977), the Court abandoned altogether " 'the use of magic words or labels' ", that "could 'disable an otherwise constitutional levy'," and "recognized that the rule against taxing the 'privilege' of doing interstate business" no longer served an analytic function. *Id.* at 284, 97 *S.Ct.* at 1081, 51 *L.Ed.*2d at 334 (quoting *Railway Express Agency v. Virginia,* 358 *U.S.* 434, 441, 79 *S.Ct.* 411, 416, 3 *L.Ed.*2d 450, 456 (1959)). Because "[t]he Court long since had recognized that interstate commerce may be made to pay its way," *Complete Auto Transit, supra,* 430 *U.S.* at 284, 97 *S.Ct.* at 1082, 51 *L.Ed.*2d at 334, the Court shifted the focus of analysis to "the question whether the tax produces a forbidden effect." *Id.* at 288, 79 *S.Ct.* at 1084, 51 *L.Ed.*2d at 337.

Having replaced formalisms with economic reality, the Court developed a simpler, more straightforward approach based on the analysis of the effects of a tax, and will sustain a tax against a Commerce Clause challenge

> when the tax is applied to an activity with a substantial nexus with the taxing State, is fairly apportioned, does not discriminate against

> interstate commerce, and is fairly related to the services provided by the State. [*Id.* at 279, 79 *S.Ct.* at 1079, 51 *L.Ed.*2d at 331.]

The Court has used this test interchangeably to test Due Process challenges to state taxation as well. *See, e.g., ASARCO, Inc. v. Idaho State Tax Comm'n,* 458 *U.S.* 307, 316-19, 102 *S.Ct.* 3103, 3108-3111, 73 *L.Ed.*2d 787, 795-96 (1982).

In its most recent pronouncement, *Container Corp. of America v. Franchise Tax Bd.,* 463 *U.S.* 159, 103 *S.Ct.* 2933, 77 *L.Ed.*2d 545 (1983), the Court combined its analysis of both Due Process and Commerce Clause challenges. The Court reviewed and summarized its development of the law. Beginning with the premise that Justice Brandeis made in *Underwood* that a state may not "tax value earned outside its borders," *Container, supra,* 463 *U.S.* at 164, 103 *S.Ct.* at 2939, 77 *L.Ed.*2d at 552, the Court explained that formal and transactional accounting, limiting values to one situs, does not reflect economic reality. The problem it sees "is that formal accounting is subject to manipulation and imprecision, and often ignores or captures inadequately the many subtle and largely unquantifiable transfers of value that take place among the components of a single enterprise. *See generally Mobil Oil Corp.,* 445 *U.S.* at 438-439, 100 *S.Ct.* 1223, 63 *L.Ed.*2d 510, and sources cited." *Id.* at 164, 100 *S.Ct.* at 2940, 77 *L.Ed.*2d at 553. These transfers of value had long been measured in the case of interstate business such as railroads, utilities or freight lines by the "unit rule." J. Hellerstein, "State Taxation Under the Commerce Clause: The History Revisited," *The State Corporation Income Tax, Issues in Worldwide Unitary Combination* 53, 65 (C. McClure, Jr. ed. 1984). Thus, a share of the value of railroad rolling stock could be apportioned to a state on the basis of track mileage there. Such an enterprise

connected physically and by "unit[y] of use and management" possessed an instate value "in combination and from use in connection with the property and capital elsewhere" in excess of the bare value of the track or line. *Adams Express Co. v. Ohio State Auditor,* 165 *U.S.* 194, 222, 41 *L.Ed.* 683, 695 (1897).

In keeping with the premise of such measures, the Court has recognized the unitary business/formula apportionment method as an acceptable approach to the problem of taxing businesses operating in more than one jurisdiction.

> It rejects geographical or transactional accounting, and instead calculates the local tax base by first defining the scope of the "unitary business" of which the taxed enterprise's activities in the taxing jurisdiction form one part, and then apportioning the total income of that "unitary business" between the taxing jurisdiction and the rest of the world on the basis of a formula taking into account objective measures of the corporation's activities within and without the jurisdiction. [*Container, supra,* 463 *U.S.* at 165, 103 *S.Ct.* at 2940, 77 *L.Ed.*2d at 553.]

In general, the formula determines a taxpayer's income tax base within a particular state by the average ratio of:

$$\frac{\text{Receipts in state}}{\text{Receipts everywhere}} + \frac{\text{Property in state}}{\text{Property everywhere}} + \frac{\text{Payroll in state}}{\text{Payroll everywhere.}}$$

That ratio applied to the taxpayer's total taxable income from all sources, yields the income attributable to the state.

This method has now gained wide acceptance, and is, in one of its forms, the basis for the division of income for state taxation of interstate commerce in forty-five states. *See Report of General Accounting Office,* "Key Issues Affecting State Taxation of Multijurisdictional Corporate Income Need Resolving," (July 1, 1982) (The Comptroller General). The method is the "benchmark against which other apportionment formulas are judged." *Container, supra,* 463 *U.S.* at 170, 103 *S.Ct.* at 2943, 77 *L.Ed.*2d at 556.

We therefore must set forth with precision the only restraints that the Supreme Court has imposed upon a state employing the unitary business/formula apportionment method of taxation of interstate businesses.

> The Due Process and Commerce Clauses of the Constitution do not allow a State to tax income arising out of interstate activities—even on a proportional basis—unless there is a " 'minimal connection' or 'nexus' between the interstate activities and the taxing State, and 'a rational relationship between the income attributed to the State and the intrastate values of the enterprise.' " *Exxon Corporation v. Wisconsin Dept. of Revenue,* 447 US, at 219-220, 65 L Ed 2d 66, 100 S Ct 2109, quoting *Mobil Oil Corp. v. Commissioner of Taxes,* 445 US, at 436, 437, 63 L Ed 2d 510, 100 S Ct 1223. [*Id.* at 165, 103 *S.Ct.* 2940, 77 *L.Ed.2d* at 553.]

Appendix A

A.

Finding the "Nexus" or "Minimal Connection"

In the classic context, let us say, of an oil company, refining its product in New Jersey and selling it in Pennsylvania, there is little difficulty in finding the "nexus." But in the more complex business organizations of today that may engage in multiple lines of endeavor, as, for example, an oil company that also sells office products and motion pictures, finding the nexus is less clear. But one thing remains constant. If the business is unitary, the taxing authority is not constitutionally required to unravel the conglomerate structure. All that the Constitution requires is:

> (1) *that a State not tax a purported "unitary business" unless at least some part of it is conducted in the State* * * *;
>
> (2) *that there be some bond of ownership or control uniting the purported "unitary business;" [and]*
>
> (3) *that the out-of-State activities of the purported "unitary business" be related in some concrete way to the in-State activities* * * *.
>
> (The functional meaning of this requirement is that there be some sharing or exchange of value not capable of precise identification or measurement—beyond the mere flow of funds arising out of a passive investment or a distinct business operation—which renders formula apportionment a reasonable method of taxation.) [*Container,*

supra, 463 *U.S.* at 165, 103 *S.Ct.* at 2940, 77 *L.Ed.2d* at 553-54 (emphasis, numeration and parentheses added).]

In the highly complex series of cases that preceded *Container,* dealing largely with taxation of income from worldwide operations of overseas subsidiaries of corporations doing some instate business, the Court disagreed on the application of the principles that determine whether a "unitary business" has been found. *See, eg., ASARCO, supra,* 458 *U.S.* 307, 102 *S.Ct.* 3103, 73 *L.Ed.2d* 787; *F. W. Woolworth Co. v. Taxation and Revenue Dep't of New Mexico,* 458 *U.S.* 354, 102 *S.Ct.* 3128, 73 *L.Ed.2d* 819 (1982); *Exxon Corp. v. Wisconsin Dep't of Revenue,* 447 *U.S.* 207, 100 *S.Ct.* 2109, 65 *L.Ed.2d* 66 (1980).

Notwithstanding repeated invitations, Congress, with the one exception of the Interstate Income Act, *Pub.L.No.* 86-272, has declined to step in to resolve the problems of federalism under its Commerce Clause powers.[1] In *Container, supra,* the Court

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1. In response to *Portland Cement Co., supra,* 358 *U.S.* 450, 79 *S.Ct.* 357, 3 *L.Ed.*2d 421, Congress enacted Public Law No. 86-272, establishing minimum jurisdictional requirements for a state to impose a net income tax on nondomiciliary corporations' income derived from interstate commerce. The law prohibits states from taxing income of out-of-state sellers of tangible personal property if their sole instate activity consists of soliciting orders to be approved outside the state and filled by delivery from a location outside the state.

At about the same time, the states were themselves taking steps to modify their existing tax apportionment schemes. In the late 1950's, representatives from the states met to discuss a uniform system and, in 1957, the Uniform Division of Income for Tax Purposes Act (UDITPA), 7A *U.L.A.* 91 (1978), was adopted by the Commissioners on Uniform State Laws and the American Bar Association. It was designed as a model act to aid states in enforcing taxpayer

(Cont'd)

appeared resolved to take itself out of the business of being a tax commission and made it clear that the taxpayer has the "distinct burden of showing by 'clear and cogent evidence' that [the state tax] results in extraterritorial values being taxed . . . ." 463 *U.S.* at 164, 103 *S.Ct.* at 2939, 77 *L.Ed.*2d at 552 (quoting *Exxon Corp., supra,* 447 *U.S.* at 221, 100 *S.Ct.* at 2119, 65 *L.Ed.*2d at 80), and that the only restraints that it will impose are "to determine whether the state court applied the correct standards to the case; and if it did, whether its judgment was 'within the realm of a permissible judgment'." 463 *U.S.* at 176, 103 *S.Ct.* at 2946, 77 *L.Ed.*2d at 560.

(Cont'd)

compliance and eliminating the possibility of double taxation of interstate businesses. UDITPA divides corporate income into nonbusiness income, for which specific allocation is permitted, and business income, for which an apportionment formula is used. For business income, UDITPA offers the traditional apportionment formula based on three factors: payroll, sales, and property.

In 1964, a congressional subcommittee published what is known as the Willis Report, a study on state taxation of interstate business. *See* "State Taxation of Interstate Commerce," *H.R.Rep. No. 1480* (88th Cong., 2d Sess., 1964). The Report criticized the diversity in state apportionment formulas and recommended a federal allocation plan using a two-factor (property and payroll) formula. The Report prodded the states to police themselves.

The product of the states' initiative was the Multistate Tax Compact. The constitutionality of the Tax Compact was upheld in *United States Steel Corp. v. Multistate Tax Comm'n,* 434 *U.S.* 452, 98 *S.Ct.* 799, 54 *L.Ed.*2d 682 (1978).

Some twenty-three states, plus the District of Columbia, have adopted the Tax Compact. Despite the Compact's goal of achieving some degree of national uniformity, however, diverse state apportionment methods abound even after the promulgation of this uniform act. New Jersey has never joined the Compact. For detailed history from which this recital is drawn, *see* K. Bakewell, "State Tax Apportionment", 48 *Mo.L.Rev.* 719 (1983).

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B.

Finding the Rational Relationship

This issue will frequently present a difficult issue for disposition. Basically, if there is a nexus, this part of the due process test comes down to the fairness of the apportionment: "whether the state apportionment formula is doing the job it was developed to do." Note, "The Unitary Tax Method," 15 *Pac. L.J.* 109, 135 (1983). In each case the resulting tax liability must not be "out of all appropriate proportion to the business transacted" in the taxing state itself. *Hans Rees', supra,* 283 *U.S.* at 135, 51 *S.Ct.* at 389, 75 *L.Ed.* at 908 (attributing 80% of income to North Carolina when only 17% warranted). Such cases frequently raise concern for double taxation when differing states use differing formulas. *See Moorman Mfg. Co. v. Bair,* 437 *U.S.* 267, 98 *S.Ct.* 2340, 57 *L.Ed.*2d 197 (1978) (taxpayer failing to meet burden of proving Iowa's single factor apportionment formula, based solely on sales, produced unreasonable results).

It should be noted that the taxpayers do not contend that the tax here is discriminatory against interstate businesses or that it is an undue burden on interstate commerce. They did not challenge the allocation formulas as being unfair as applied to an interstate business like their own, and they do not suggest that the result of the New Jersey tax is multiple taxation elsewhere. Indeed, they do not at all attack the amount of taxes determined by the Director, choosing to rely solely upon their unitary business arguments. We must therefore analyze the New Jersey tax at issue and consider whether the taxpayer has presented clear and cogent evidence that the items of income and receipts were not part of its "unitary business," and that application of the tax results in "extraterritorial values being taxed."

Appendix A

II.

The State Tax

The Corporation Business Tax Act, *N.J.S.A.* 54:10A-1 to -40, enacted in 1945, requires that a corporation shall pay an annual franchise tax (Corporation Business Tax or CBT) "for the privilege of having or exercising its corporate franchise in this State, or for the privilege of doing business, employing or owning capital or property, or maintaining an office, in this State." *N.J.S.A.* 54:10A-2.

The history of the act has been detailed in this Court's earlier decisions. *See Roadway Express, Inc. et al. v. Director, Div. of Taxation,* 50 *N.J.* 471 (1967); *United States Steel Corp. v. Director, Div. of Taxation,* 38 *N.J.* 533 (1962). It will suffice to summarize that history. Originally enacted to replace the "tax lightning" inflicted by local levies on intangible property, the 1945 tax was limited to the "net worth" of the corporations.[2] The net income measure of the tax, as another element in addition to net worth, was inserted by *L.* 1958, *C.* 63. In essence, the latter is a corporate income tax, although at the time denominated a franchise tax due to a surmised "historical antipathy in New Jersey to an income tax as such." *Roadway Express, supra,* 50 *N.J.* at 485.

For corporations that maintain a regular place of business outside of New Jersey, the act recognizes that only a percentage of the taxpayer's net worth and net income may be the result of its activities in the state. Consequently, an "allocation formula"

2. *See Fedders Fin. Corp. v. Director, Div. of Taxation,* 96 *N.J.* 376 (1984), for the meaning of "net worth." The Legislature has since passed a phased out repeal of the "net worth" provisions of the act. *L.* 1982, c. 55.

is applied to both the net worth and net income tax bases so that only those portions of entire net worth and entire net income, respectively, that are fairly attributable to the corporation's activities in New Jersey, are used in the measure of the tax. *See N.J.S.A.* 54:10A-6. The allocation formula consists of three factors, namely, property, payroll and receipts. Each of the three factors in the so-called three-ply formula is expressed as a fraction, the numerator of which is, respectively, the taxpayer's New Jersey property, receipt, and payroll; and the denominator of which is the taxpayer's total property, receipts, and payroll generated by the operations of the entire corporation. *N.J.S.A.* 54:10A-6(B). These fractions are averaged, and the combined fraction (referred to in New Jersey as the allocation factor) is then applied to the taxpayer's entire net worth and entire net income in order to determine the percentage or portion of net worth and income properly attributable, and thus, taxable to New Jersey. *See Metromedia, Inc. v. Director, Div. of Taxation,* 97 *N.J.* 313 (1984).

This appeal focuses upon the net income tax base.[3] New Jersey defines the taxpayer's "entire net income" in terms of its federal "taxable income," with certain exceptions to be noted. *N.J.S.A.* 54:10A-4(k). To this base, New Jersey applies its tax. An example will illustrate the tax's effect. Assume that a Pennsylvania manufacturing corporation, subject to the CBT, markets its products in New Jersey and New York; that its property is only

3. In its petition of appeal to the Tax Court, Silent Hoist also challenged the inclusion of its portfolio income in net worth. Technically, a claim for refund would have to be made since the taxpayer's original return had included it in net worth. The reasons that we furnish for net income taxation would be applicable to net worth analysis. Since that tax has been repealed, we focus the opinion on net income.

in Pennsylvania; that its receipts are equal in the three states; and that its payroll is 50% in Pennsylvania, 25% in New York and 25% in New Jersey. If the company's taxable income were $500,000, the New Jersey CBT on net income would be calculated as follows:

	Property	Receipts	Payroll		Average Ratio of	
NJ	0	33	25	58		
Total	100	100	100	100	÷ 3	= 19.3% (Allocation Formula)

(19.3%)	×	($500,000)	×	(9%)	=	$8,685
Allocation Factor		Entire Net Income		Tax Rate		Tax

The effective tax rate in New Jersey is thus reduced to 1.7% of entire net income by the application of the formula. If each of the other states followed a comparable taxing scheme, the overall tax would be fair and fairly apportioned.

As noted, New Jersey has eschewed joining the Multistate Tax Commission.

> New Jersey follows the principle of apportioning all income under its three-factor formula. No provision is made for specifically allocating any income, such as interest, dividends, capital gains, patents and copyrights, rentals, income from services, and the like, which is the practice in many States, Under the Uniform Division of Income for Tax Purposes Act (UDITPA), which has been

> adopted by 24 States and the District of Columbia, this type of income is taken out of the apportionment formula, and is specifically allocated.[4] [*Report of the New Jersey Tax Policy Committee,* Part V, "Non-Property Taxes in a Fair and Equitable Tax System," (February 23, 1972) at 25 (Cahill Commission).]

Careful study has been made of the question whether New Jersey should modify its policy on allocation of income but the New Jersey Tax Policy Committee recommended that the policy of treating all items of income within the apportionment formula be continued. *Id.* at 27. Consequently, we lay great stress upon the broad authority the act gives to the Director to adjust the allocation factor in order to reflect more accurately and fairly "the activity, business, receipts, capital, entire net worth or entire net income of a taxpayer" reasonably referable to the state. *N.J.S.A.* 54:10A-8. *N.J.S.A.* 54:10A-8 authorizes the Director to make specific adjustments: (1) to adhere to those factors already set forth in the statutory formula, namely, property, receipts, and payrolls; (2) to include in the formula one or more other acceptable recognized factors, such as expenses, purchases, or existing contracts; and (3) to exclude one or more assets from the formula or from the entire net worth tax base. In addition to this specific authority, the Director is given broad general discretion to "apply [ ] any other similar or different method calculated to effect a

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4. While not specifically allocating dividends, New Jersey is generous in its treatment of such income. This will be significant in our consideration of the taxpayer's investment income. In New Jersey, only 50% of the dividends received from non-subsidiaries are included in the measure of the net income tax, and dividends from subsidiaries (at least 80% owned) are totally excluded from the tax base. *N.J.S.A.* 54:10A-4(k)(1).

fair and proper allocation of the entire net income and the entire net worth reasonably attributable to the State." *N.J.S.A.* 54:10A-8(e). *See Metromedia, Inc., supra,* 97 *N.J.* 313.

With this as background, we examine how the Director applied the act to the taxpayer.

III.

The Taxpayer and Its Operations

Silent Hoist and Crane Co., Inc. is a New York corporation having its principal place of business and its manufacturing plant in Brooklyn, New York. It owns two parcels of commercial property in New Jersey, one in Clifton and one in Bloomfield. It originally intended to move its plant to Clifton but abandoned the idea. Silent Hoist obtained a certificate of authority and qualified to transact business in New Jersey under *N.J.S.A.* 14A:13-3 during the relevant years. None of its real estate tenants were related to the manufacturing operation. Its sales to customers in New Jersey for the relevant years in comparison to total sales and services as shown on its books of account were:

	1971	1972	1973	1974
New Jersey	436,566	986,862	998,740	706,410
Total	5,104,500	5,472,660	6,672,307	6,111,811[5]

When it filed its New Jersey CBT returns for the period, it reported no income from sales but reported only the income

5. These figures are not intended to be exact. The income shown is a composite of sales and services. The illustration serves only to demonstrate the approximate relationship of the New Jersey sales to system-wide operations.

and expenses related to its New Jersey real estate operations.[6] Upon audit, the Division of Taxation, noted that the taxpayer had failed to report its "entire net income," equated with taxable income, and consequently increased Silent Hoist's net income to include its sales income and the income from its investments. (As noted, New Jersey only includes 50% of dividends received from other corporations.)[7]

The taxpayer appealed the assessment to the Tax Court. The trial developed the following facts. Silent Hoist is a privately held corporation. Its president, Eric Wunsch, is its principal manager. He exercises effective control over all areas of the company's operations. Its mode of operation was to seek out potential customers in New Jersey and elsewhere. The company's employees would visit potential customers to survey their needs. They would advise the customer of a possible solution to the material handling problems and suggest the superior quality of the Silent Hoist product. If the customer's interest grew, design conference would follow either in Brooklyn, New Jersey, or at a location having a similar piece of plaintiff's machinery.

Following the design phase, the machinery would usually be fabricated in Brooklyn or, in some cases, in Connecticut, and be delivered to New Jersey. The company's sales representatives were themselves engineers and would follow up if one of the machines malfunctioned. The representatives would show the

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6. The taxpayer included in its entire net worth both its Brooklyn manufacturing plant and the investment securities that are at issue.

7. The Division made two other adjustments, tó show the securities at market value and to correct the allocation factor. Neither is the subject of this appeal.

customer's personnel how to deal with problems, and on occasion themselves remove pieces of the machine and ship them back to the plant for repairs. The company's service department performed warranty repairs, trained customer personnel, and reviewed technical problems with the customers.

Wunsch described himself as the general manager whose duty it was to keep "the business functioning and working profitably." He supervised and directed all of the company's activities. He made the real estate and investment decisions, and he was involved in the design of the machinery and its sales, advertising and long-range planning.

The taxpayer had one bank account that covered all of its activities. All receipts went into and most expenses were paid out of the account. There was a single chart of accounts for the business with no separate accounts for manufacturing, sales, real estate or securities investment.

The central issue before the Tax Court was whether this was a "unitary business." That court believed that existing Supreme Court precedent required that it hold for the taxpayer, that its investment, real estate, and sales businesses were distinct and could not be taxed under a unitary business/formula apportionment system. It entered judgment in favor of the taxpayer. 5 *N.J. Tax* 242 (1983). At the time of the Tax Court decision, *ASARCO* was the last Supreme Court pronouncement. As seen in Part I(A.) hereof, *supra*, (slip op. at 7), the Supreme Court has since modified its holding in *ASARCO*.

The Appellate Division affirmed on the basis of the Tax Court opinion. 6 *N.J. Tax* 348 (1984). We granted the State's petition for certification. 97 *N.J.* 650 (1984).

Appendix A

IV.

A.

Was Silent Hoist's Portfolio Income Correctly Included in Its Apportioned Income Base?

The "linchpin of apportionability" is the finding of a "unitary-business." *Mobil Oil Corp. v. Commissioner of Taxes of Vermont,* 445 *U.S.* 425, 439, 100 *S.Ct.* 1223, 1232, 63 *L.Ed.* 2d 510, 522 (1980). If ever there was a unitary enterprise, this appears to be one. The taxpayer has sought to rely upon two 1982 decisions of the Supreme Court: *ASARCO, supra,* 458 *U.S.* 307, 102 *S.Ct.* 3103, 73 *L.Ed.*2d 787; and *Woolworth, supra,* 458 *U.S.* 354, 102 *S.Ct.* 3128, 73 *L.Ed.*2d 819. Both of these cases are remote from *Silent Hoist* in terms of the economic transactions. In each case, the primary issue was that the taxing state sought to include in the taxpayer's base the income, not of the taxpayer, but of foreign subsidiaries not doing any business in the taxing state by taxing the dividends received from the subsidiaries. (*ASARCO* also dealt with income from portfolio investments, to be discussed in fn. 8, *infra,* (at 22)). Here we deal not with consolidated returns, income of subsidiaries or foreign commerce issues. We deal with one entity, Silent Hoist. Concededly, one such entity may not be unitary. But it is a rare case.

The Supreme Court has never adopted a single test for determining what is a unitary business. A commentator has described the Court as "adher[ing] to its catholic approach by stressing a number of factors, many of them familiar" for determining when a business is unitary. W. Hellerstein, "State Income Taxation," 79 *Mich.L.Rev.* 113, 150 (1980). In *Container,*

supra, the Court reemphasized that the "final point that needs to be made about the unitary business concept is that it is not, so to speak, unitary." 463 *U.S.* at 167, 103 *S.Ct.* at 2941, 77 *L.Ed.*2d at 554-55. However, under any test that has been approved, the taxpayer meets the measure of a unitary business.

Silent Hoist meets the test, in *Exxon* terms, of enjoying the "benefits from an umbrella of centralized management and controlled interaction." 447 *U.S.* at 224, 100 *S.Ct.* at 2120, 65 *L.Ed.*2d at 81. The interaction between the various aspects of plaintiff's business need not involve measurable flows of cash. Rather, the question is whether there have been "unquantifiable transfers of value * * * among the components of a single enterprise." *Container, supra,* 463 *U.S.* at 164, 103 *S.Ct.* at 2940, 77 *L.Ed.*2d at 553.

Silent Hoist meets the *Butler Bros.* test of three unities of ownership, operation, and use. Unity of ownership means that the activities outside the tax jurisdiction, together with the in-state activities are owned by the same taxpayer; unity of operation means that there is a centralized executive structure with central purchasing, advertising, accounting and management; and unity of use is found in a centralized executive force and a general system of operations. *See Butler Bros. v. McColgan,* 17 *Cal.*2d 664, 111 *P.*2d 334 (1941), aff'd, 315 *U.S.* 501, 62 *S.Ct.* 701, 86 *L.Ed.* 991 (1942).

Silent Hoist also meets the "dependent upon or contributory" test. *See Ramsay, Scarlett & Co., Inc. v. Comptroller,* 302 *Md.* 825, 490 *A.*2d 1296 (1985) (test not met in circumstances); *F.W. Woolworth Co. v. Director, Div. of Taxation,* 45 *N.J.* 466 (1965); *Crawford Mfg. Co. v. State Comm'n of Revenue and Taxation,*

180 *Kan.* 352, 357, 304 *P.*2d 504, 510 (1956). This concept is closely related to the concept of "mutual benefit." *Western Auto Supply Co. v. Commissioner of Taxation,* 245 *Minn.* 346, 357, 71 *N.W.*2d 797, 805 (1955).

Applying each of the above enumerated tests, and bearing in mind that the taxpayer has the burden of proof, *Mobil, supra,* 445 *U.S.* at 439-40, 100 *S.Ct.* at 1232-1233, 63 *L.Ed.*2d at 522, it is clear from this record that the taxpayer has made no showing that its business falls without the tests. Here, as noted, and as distinct from the Supreme Court cases in which multinational corporations and their subsidiaries were involved, we are discussing only one corporation, Silent Hoist. It is for this reason that the divident payor v. divident recipient test enunciated by the Supreme Court in *Mobil, Exxon, ASARCO, Woolworth* and *Container* are relied upon by Silent Hoist is not applicable. In those cases the question involved, for the most part, dividends paid from major subsidiaries to their parent. The inquiry was whether the parent, the recipient of the dividend income, controlled the subsidiary, the divident payor. The test to be developed here involving one corporation is whether the unities apply within the internal operations of Silent Hoist. The focus must be on Silent Hoist's investment activity and other aspects of its corporate business and the role the investment activity plays in those other activities.

First, the record establishes that all of Silent Hoist's business is controlled by one chief executive officer, Mr. Wunsch, who testified that he made all the major corporate decisions regarding manufacturing, real estate, and investment. What emerges from the record is a corporation run and controlled by one man. Wunsch managed the company with the assistance of a vice-president in

charge of sales and another in charge of engineering. Thus, Wunsch's involvement in the three aspects of the business was evident. On a far less substantial showing of centralized management, the Supreme Court of Montana held in *Russell Stover Candies, Inc. v. Dep't of Revenue,* 665 *P.*2d 198 (Mont.1983) that the taxpayer's in-state cattle ranch divisions and out-of-state paper box divisions formed parts of a unitary business. *See also Commissioner of Revenue v. Associated Dry Goods, Inc.,* 347 *N.W.*2d 36 (Minn.1984), *cert.* den., ____ *U.S.* ____, 105 *S.Ct.* 124, 83 *L.Ed.*2d 66 (1984) (separate divisions formed a unitary business where corporation had a single board of directors and a single set of officers and shareholders, administrative services were centralized, and there was a commingling of funds); *ARMCO, Inc. v. Hardesty,* 303 *S.E.*2d 706 (W.Va.1983), rev'd on other grounds, ____ *U.S.* ____, 104 *S.Ct.* 2620, 81 *L.Ed.*2d 540 (1984) (activities of steel group, wire rope group, and metal products division are parts of "unitary business").

Here, the evidence does not establish that any of the alleged operations were conducted as a discrete business enterprise. Clearly, the investment operation was not a discrete business enterprise; it was merely incidental to the company's manufacturing business. Also, the real estate in New Jersey never was a separate and discrete business operation from the investment or manufacturing aspect of the business. The Clifton site was originally purchased by Silent Hoist to be the new location of its manufacturing business which it contemplated moving from New York City. The building was completed in 1971. Wunsch exercised control over the building before it was leased. Moreover, presumably, the funds used to purchase the property were derived from general corporate funds, including the manufacturing business, or from the sale of securities. From Silent Hoist's financial records, it appears that the Bloomfield real estate was

not rented during certain of the tax years in question; thus, presumably, the substantial expenses for that operation were paid out of general corporate funds.

The financial records of the company offer strong evidence that the real estate, investment and manufacturing business were closely integrated and run as a unitary business. There was one bank account for the entire corporation, into which all receipts were deposited and out of which nearly all expenses were paid. There was a direct monetary flow of value from one segment of the business to another.

The source of funds and application of funds also establish the integration of the business. From the financial records, it appears that the proceeds of securities liquidated. added to the corporation's single bank account, were used as working capital in the manufacturing aspect of the business and to buy New Jersey property and presumably to service the debt on it; and that the corporation's centralized administrative services, included the preparation of tax returns and financial statements for the real estate business. Furthermore, in filing its New York Corporation Franchise Tax Return on a unitary basis, Silent Hoist made use of its New Jersey real estate depreciation allowance and losses to offset its manufacturing and investment income. The real estate depreciation provided substantial cash flow benefits for the entire business.

We agree with Silent Hoist that a corporation will not be deemed a unitary corporation merely because the income from a subsidiary or a division adds to the richness of the corporation, or that the occasional oversight with respect to capital structure, debt and dividends that a parent gives a subsidiary is enough to establish a unity relationship, or that the single set of accounting

records of the corporation will be sufficient to establish a unitary business. We do not hold that any of these factors alone would be sufficient to find that Silent Hoist is a unitary corporation. Rather, we hold that it is the combination of these factors which leads indisputably to the conclusion that Silent Hoist is a unitary corporation.

New Jersey, like the United States Supreme Court, has been eclectic in its approach to the several tests for finding a unitary business. *See Woolworth, supra,* 45 *N.J.* 466. What we focus on here, as did the *Woolworth* Court, is economic reality. All that the Supreme Court asks is that we assure ourselves that there be "some sharing or exchange of value not capable of precise identification or measurement—beyond the mere flow of funds arising out of a passive investment or a distinct business operation." *Container, supra,* 463 *U.S.* at 166, 103 *S.Ct.* at 2940, 77 *L.Ed.*2d at 554.

As we have seen, Silent Hoist's investment capital was capable of being pledged, liquidated or converted to other uses of the company's sales or real estate operations. To describe this economic power as passive does not reflect economic reality.

The taxpayer would have us divide this investment income from the organic whole of the business enterprise. This is however, not a matter of constitutional law, but a matter of tax preference. Our job is not to rewrite the State's Corporation Business Tax but to apply it as intended. New Jersey's tax policy is quite distinct from the majority of states. We do not seek to allocate non-business income to the place of commercial or legal domicile. On the other hand, we accommodate our tax policy to the modern business complex by specifically excluding all dividends from

subsidiaries (at least 80% owned) and 50% of other dividend income.[8]

We are more than satisfied here that there was a distinct sharing of the value of common management, accounting and operations that takes the portfolio income of this taxpayer well within the concept of a unitary business.

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8. Indeed, had the *ASARCO* facts arisen in New Jersey, the issues would not have been the same because New Jersey automatically excludes 50% of dividend income and does not employ combined or consolidated accounting. In *ASARCO,* Justice Powell took pains in a footnote to explain that investment income may be taxed by non-domiciliary states. *See* 458 *U.S.* at 328 n. 22, 102 *S.Ct.* at 3114 n. 22, 73 *L.Ed.*2d at 802 n. 22. *ASARCO* can only be understood by recognizing what the taxing state was trying to do. Idaho wanted to have it both ways; it wanted to include the subsidiaries' income in the Idaho income base, but refused to include the property, payroll and receipts of the subsidiaries in the denominator of its formula. The result was a severe distortion. Commentators have recognized that this tortuous distinction led to an indefensible position of advocacy that foreclosed its case. *See, e.g.,* C. Floyd, "The 'Unitary' Business in State Taxation: Confusion at the Supreme Court?" 1982 *B.Y.U.L.Rev.* 465 (1982). The Supreme Court, in the commentator's opinion, was led to confuse the issues of apportionment of "business income" under UDITPA with the links necessary to justify imposition of a state tax on a unitary business. Floyd, *supra,* 1982 *B.Y.U.L.Rev.* at 481. By emphasizing that the five dividend-paying companies were not part of ASARCO's unitary business, Idaho "no doubt intended to lay the foundation for a holding that no adjustment of the factors of apportionment was necessary * * * ." *Id.* at 501. The gamble was fatal to Idaho's position and gave ASARCO the victory that Mobil lost because it had failed to timely raise the question of apportionment. *See Mobil, supra,* 445 *U.S.* 425, 100 *S.Ct.* 1223, 63 *L.Ed.*2d 510. It was this distortion that led to Justice Stevens' dissent in *Mobil.* He recognized the constitutional power of states to tax all income of a unitary business, including investment income, provided that the formula for including all such combined and subsidiary income was fair. 445 *U.S.* at 449-50, 100 *S.Ct.* at 1237-1238, 63 *L.Ed.*2d at 529.

(Cont'd)

Appendix A

B.

Was Silent Hoist's sales income correctly included in its tax base?

The same reasons that impel us to find the taxpayer's portfolio income part of its unitary business apply with equal force to its sales income. Its New Jersey sales were more than $3,000,000, or almost 13% of system sales of $23,361,278. *See supra* (at 15). As such, they contributed significantly to the enhanced value of the unitary business. These sales were a significant source of the funds that enabled the taxpayer to acquire its property in New Jersey.

We perceive the same factors at work as in the case of the portfolio income. The centralized one-man management team that coordinated the real estate operations in New Jersey, as well as the portfolio investments, oversaw the sales operation. Depreciation from the New Jersey operation played a role in the tax returns of sales activities. We find that there were transfers of value among the components of the enterprise, an umbrella of centralized management and controlled interaction, and a dependence and contribution among the operations creating a mutual benefit that each shared.

(Cont'd)

New Jersey's tax scheme as applied to Silent Hoist falls convincingly short of any such distortion. We place great emphasis upon the fact that the receipts fraction must be determined in harmony with the definition of entire net income. "To put it differently, the tax base and the receipts fraction are symmetrical. That which is excluded from the former is excluded from the latter and, conversely, that which is included in the former is also included in the latter." *American Tel. & Tel. v. Taxation Div. Director,* 4 *N.J. Tax* 638, 648 (1982). Thus, our elimination of 80% owned subsidiary income and 50% of all dividend income serves to harmonize the fractions.

Moreover, even were Silent Hoist's sales not considered part of its unitary business, there would be little doubt that there is an otherwise sufficient "minimal connection" with the state that warrants the assessment. *See Tamko Asphalt Products, Inc. v. Taxation Div. Director,* 5 *N.J. Tax* 446 (1983), aff'd, 6 *N.J. Tax* 342 (App. Div. 1984). In that case a Maryland asphalt roofing supplier contested a CBT assessment. Tamko did not advertise in New Jersey, had no bank account, inventory, plant or telephone listing and no identifiable office. Yet, the Tax Court found that its marketing activities in New Jersey distinctly exceeded the bare "solicitation of orders" for which "the Interstate Income Act, *Pub.L.No.* 86-272, prohibits imposition of a state tax measured by income on corporations engaged only in the solicitation of orders within the taxing state." 5 *N.J. Tax.* at 456. The court explained that Tamko's sales representatives, one of whom lived in New Jersey, not only solicited orders but "also promote[d] Tamko products and service customer accounts by investigating, reporting and adjusting customer complaints." *Id.* It found Tamko to be subject to tax in New Jersey. *Id.* at 453-54. In view of the disposition that we make of the unitary business issue, we need not base our decision on these contacts although we note their similarity. Hence, because the sales income of Silent Hoist is part of its unitary business conducted in New Jersey through its real estate ventures, that sales income, fairly apportioned, is part of the taxpayer's entire net income.

V.

The Court, having concluded that there is an adequate "nexus or minimal connection" between the State and items of income, the only question remaining is whether the tax has been "fairly apportioned." *Container, supra,* 463 *U.S.* at 171, 103 *S.Ct.* at

2943, 77 *L.Ed.*2d at 557. Although it was not the basis of its decision, the Tax Court concluded that the Director had erred in holding that he was without discretion to review bookkeeping or accounting records of the corporation to determine if, in fact, the allocation formula was unfair or unreasonable. Instead the Director reviewed only the tax returns and subsequent correspondence between the parties. The Tax Court concluded this to be an insufficient basis for the denial. As noted, before us, the taxpayer did not contest, on a statutory basis, the fairness of the allocation formula as applied to its circumstances. It chose to rely entirely upon its constitutional argument that the Tax Court sustained.

Nonetheless, indulgence of this opportunity is appropriate in this case because when the case was before the Tax Court, the parties would have approached the matter in light of the recent decisions in *ASARCO* and *Woolworth.*[9] Those decisions reflected an attitude of judicial vigilance and "at least by implication cast doubt on the power of a state to include in a nondomiciliary payee's apportionable tax base any income from intangibles received for an out-of-state payor with which the payee is not conducting a unitary business." W. Hellerstein, "State Income Taxation of Multijurisdictional Corporations, Part II: Reflections on *ASARCO* and *Woolworth,*" 81 *Mich.L.Rev.* 157, 178-79 (1982). Only the cautious would have observed that it was "not, however, the only reading it may be given, a fact that may render the preceding discussion more than academic." *Id.* at 182.

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9. *ASARCO* and *Woolworth* were decided on June 29, 1982. The Tax Court decision was decided on January 28, 1983. *Container* was decided on June 17, 1983.

The discussion became academic when

> in *Container Corp. of America v. Franchise Tax Board,* the Supreme Court significantly enhanced the states' power to tax income of domestic corporations' foreign subsidiaries. Using broad language that suggested a desire to place severe limits on future challenges to state corporate income tax schemes, the Court reversed the thrust of decisions from the previous Term. [Note, "The Supreme Court 1982 Term," 97 *Harv.L.Rev.* 70, 112 (1983) (footnotes omitted).]

The *Container* decision "implies that the Court's holdings in *Woolworth* and *ASARCO* can be confined to their specific facts." Note, "State Taxation of Multinationals and the Unitary Business Concept: A Contemporary View," 10 *Brooklyn J. of Int'l Law* 115, 145 (1984). Putting it plainly, Professor Hellerstein predicted that perhaps the most that could be drawn from *ASARCO* and *Woolworth* was that whatever broad principles may have been stated, "the unitary business in the end may simply be something that the Court knows when it sees it." Hellerstein, *supra,* 81 *Mich.L.Rev.* at 183-84.

We sincerely doubt that the Supreme Court would not know that Silent Hoist's business was unitary when it saw the facts before us. We are satisfied that the sales and investment income of Silent Hoist is subject to a fairly apportioned income tax in New Jersey.

We have always placed great reliance on the discretion of the Director to adjust the factors to compensate for any unfairness in their application. *Woolworth, supra,* 45 *N.J.* at 494-95. While

we are not persuaded that the assessment will be shown to be "out of all appropriate proportion," *Hans Rees', supra,* 283 *U.S.* at 135, 51 *S.Ct.* at 389, 75 *L.Ed.* at 908, the taxpayer should be allowed the opportunity to be heard on the question whether the formula as applied produces such results with respect to its activities in New Jersey.

The judgment of the Appellate Division is reversed and the cause remanded to the Tax Court to test the claim of proportionality.

For reversal and remandment—Chief Justice WILENTZ and Justices CLIFFORD, HANDLER, POLLOCK, O'HERN and GARIBALDI—6.

For affirmance—None.

APPENDIX B — OPINION OF THE TAX COURT OF NEW JERSEY

TAX COURT OF NEW JERSEY
DOCKET NO. MC515-77

SILENT HOIST & CRANE CO., INC.,

Plaintiff,

vs.

DIRECTOR, DIVISION OF TAXATION,

Defendant.

Decided Jan. 28, 1983

Daniel E. Horgan, for plaintiff
(Waters, McPherson, McNeill, attorneys)

Mary R. Hamill, Deputy Attorney General,
for defendant
(Irwin I. Kimmelman, Attorney General)

EVERS, J.T.C.

Silent Hoise & Crane Co., Inc. (taxpayer), a New York corporation, appeals from a deficiency assessment imposed by Director, Division of Taxation (Director) for taxes allegedly due for 1971 through 1974 under the Corporation Business Tax Act (CBT), *N.J.S.A.* 54:10A-1 *et seq.* The issue presented is whether the scope and nature of taxpayer's various business activities may be classified as "unitary" so as not to be violative of the limitations placed on state taxing powers by the Due Process Clause, U.S.

Appendix B

CONST. Amend. XIV, § 1, and as "unitary" is defined in *F.W. Woolworth Co. v. New Mexico*, ____ *U.S.* ____, 73 L. Ed. 2d. 819, 102 *S.Ct.* 3128 (1982), pet. for rehearing den. October 18, 1982, and *ASARCO, Inc. v. Idaho*, ____ *U.S.* ____ 73 L. Ed. 2d. 787, 102 *S.Ct.* 3103 (1982), pet. for rehearing den. October 18, 1982. It does appear that the precise distinguishing characteristics between "unitary" and "nonunitary" businesses have ever been clearly decided in New Jersey, therefore, enlightened by the foregoing United States Supreme Court decisions, this court will attempt to provide such clarification.

Taxpayer does not dispute the validity of CBT but does contest Director's action in imposing the tax on what taxpayer claims is extra-territorial income from its manufacturing-sales business and its investment portfolio. Taxpayer contends that its business is "nonunitary" and exempt from CBT. As such it seeks to have sales income, interest, dividends and capital gains on investment assets excluded from net income and investment assets, stocks and bonds excluded from net worth for tax computation purposes.[1] Violations of due process and of the Commerce Clause, *U.S. CONST.*, Art. I, § 8, Cl. 3 have been alleged by taxpayer.

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1. Taxpayer seeks to have the following excluded from income:

1971 — $ 762,446.49
1972 — $1,065,678.45
1973 — $1,387,339.40
1974 — $ 98,316.98

Taxpayer also seeks to have the following excluded from net worth:

1971 — $2,336,096
1972 — $3,025,688
1973 — $3,241,735
1974 — $2,236,531

(Cont'd)

Appendix B

Conversely, Director contends that its imposition of tax on taxpayer pursuant to CBT for the privilege of exercising its corporate franchise and for doing business within the state was a fair and reasonable method of allocating income and net worth for tax purposes because of the "unitary" nature of taxpayer's business and that there were no violations of taxpayer's constitutional rights.

For the reasons hereafter stated the court directs that judgment be entered in favor of taxpayer. The court finds that, except for its New Jersey real estate (the tax imposed thereon is not disputed), no credible evidence was presented to conclude that taxpayer's business, which entailed manufacturing, sales and securities investments, is subject to taxation in New Jersey.

Taxpayer's heavy equipment manufacturing plant and its principal place of business is located in Brooklyn, New York where it also maintains a diversified securities portfolio. The record indicates all securities were assembled for investment purposes and were held by a New York broker. During the period in question taxpayer also owned two parcels of industrially zoned land in Clifton and Bloomfield, New Jersey, neither of which were used in taxpayer's manufacturing business; both were rented to others. This property represented taxpayer's sole tangible connection with this state. It had no office, employees, agents or investments in New Jersey.

(Cont'd)

The resulting deficiency amounts, not including interest, sought by taxpayer to be dismissed are as follows:

1971 — $ 9,618.51
1972 — $18,832.82
1973 — $19,800.91
1974 — $ 1,089.22

Total — $49,341.46

Appendix B

The CBT Act imposes a tax on a foreign corporation for the privilege of having or exercising a corporate franchise, doing business, employing or owning capital or property or maintaining an office in New Jersey.[2] The tax is calculated on those portions of the corporation's Entire Net Worth and Entire Net Income allocable to New Jersey. *N.J.S.A.* 54:10A-2. The fundamental purpose of the apportionment provisions of *N.J.S.A.* 54:10A-1 *et seq.* and the three factor formula embodied therein is to achieve a fair apportionment to New Jersey of business conducted by a multi-state enterprise within the state. The Business Allocation Factor of CBT limits the New Jersey allocated portions of entire net worth and entire net income to amounts which are attributable to activities occurring in or related to the State of New Jersey.[3] The limitation created by the allocation factor preserves the constitutional doctrine that a state cannot impose a tax which is "not attributable to transactions within its jurisdiction". *See*

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2. Entire Net Worth has been equated with stockholders' total book equity and Entire Net Income has been labeled as federally taxable income with modifications. *See* generally, *Roadway Express, Inc. v. Director, Div. of Taxation,* 50 *N.J.* 471 (1967); *N.J.S.A.* 54:10A-5(a) and (c).

3. The allocation factor is the average of three fractions (*N.J.S.A.* 54:10A-6(1). The average value of the real and tangible personal property belonging to taxpayer within the state during the period in question divided by the average value of all such property wherever situated. (2) The receipts of taxpayer arising during the period in question from the sales of tangible personal property made to all points within the state, services performed within the state, rents and royalties from property located in the state or copyrights-patents within the state, and other business receipts earned within the state divided by the total amount of all such receipts belonging to taxpayer, wherever earned during the period. (3) Wages, salaries and other personal service compensation of officers-employees located within the state divided by wages, salaries and other compensation paid to all of the taxpayer's officers-employees during the period in question.

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Hans Rees' Sons, Inc. v. North Carolina, 283 *U.S.* 123 (1931); and *Evco v. Jones,* 409 *U.S.* 591 (1977).

> A state is not entitled to tax tangible or intangible property that is unconnected with the state* * *a state will not be permitted, under the shelter of an imprecise allocation formula or by ignoring the peculiarities of a given enterprise, to 'protect the taxing power of the state plainly beyond its borders'. *Norfolk and Western Ry. Co. v. Missouri Tax Commission,* 390 *U.S.* 317 (1968).

The thrust of the Supreme Court's decisions in *Woolworth* and *ASARCO, supra,* and two apportionment cases from the 1980 term, *Mobil Oil Corp. v. Commissioner of Taxes,* 445 *U.S.* 425 (1980) and *Exxon Corp. v. Wisconsin,* 447 *U.S.* 207 (1980) is that "the linchpin of apportionability in the field of state income taxation is the unitary-business principle". *ASARCO, supra,* at 795 quoting from *Mobil, supra,* at 439-440. These cases have further articulated limiting clarifications of the term "unitary businesses" which now make it apparent that certain types of business activities are "non-unitary" as a matter of law and can be taxed solely by the state of corporate domicile. The law mandates that the Due Process Clause insures fundamental fairness of apportioned state taxes by requiring that the particular taxpayer's business be characterized as "unitary" in nature prior to imposing the tax. *ASARCO, supra; Woolworth, supra; Clairol, Inc. v. Kingsley,* 57 *N.J.* 199 (1970), aff'g. 109 *N.J.Super.* 22 (App. Div. 1969) app. dism. 402 *U.S.* 902 (1971); *F. W. Woolworth v. Dir., Division of Taxation,* 45 *N.J.* 466 (1965).

As enunciated by the Supreme Court, there are three indicia of a unitary business; "functional integration, centralization of

management and economies of scale". *ASARCO, supra,* at 795. In making the determination of whether due process has been complied with, proof of a "sufficient nexus" between the taxing state and the particular taxpayer must be presented. An examination of the "underlying economic realities" of taxpayer's business supplements proof of this nexus and of the "unitary" and "nonunitary" nature of the business, (both within and without the state). In the instant case recourse must be had to the particular factual circumstances to determine whether taxpayer is subject to CBT. *See* generally *Pinggold Coal Mining Co. v. Dir., Division of Taxation,* 4 *N.J.Tax* 321, 332 (Tax Ct. 1982).

For the years at issue taxpayer reported and paid net worth taxes in the respective amounts of $3,535.83 in 1971, $4,222.49 in 1972, $4,096.53 in 1973 and $4,082.86 in 1974. Taxpayer paid no net income tax during this period. In computing its business allocation factor for schedule K of the CBT return taxpayer reported percentages of 29.06%, 32.02%, 28.19% and 27.94% for 1971 through 1974 respectively. To alleviate what it claimed was an unjust result from a strict application of the statutory formula, taxpayer used only the income from its real estate operations in computing the net income tax portion of schedule A of its CBT return. These net income amounts were reported as ($129,614.31) for 1971, ($103,357.82) for 1972, ($49,822.15) for 1973 and ($21,689.31) for 1974. Taxpayer submitted an attachment to the returns explaining its adjustment of the net income to reflect only the real estate holdings in New Jersey. Director rejected taxpayer's adjustment, conducted an audit and found taxpayer liable for corporate business taxes as follows:

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	1971	1972	1973	1974
Net Worth Tax	$3,686.60	$ 4,635.93	$ 4,355.33	$3,677.17
Net Income Tax	$9,467.74	$18,419.38	$19,542.11	$1,494.91

As noted earlier, deficiencies were assessed against taxpayer in the following amounts.

1971	1972	1973	1974
$9,618.51	$18,832.82[4]	$19,800.91	$1,089.22

The total tax assessment is $50,633.31, not including interest, of which $49,341.46 is contested.

Taxpayer filed a formal petition with the Director for adjustment pursuant to *N.J.S.A.* 54:10A-8 which statute provides:

> If it shall appear to the Commissioner that an allocation factor determined pursuant to § 6 does not properly reflect the activity, business, receipts, capital, entire net worth or entire net income of a taxpayer reasonably attributable to the state, he may adjust it by:
>
> (a) Excluding one or more of the factors therein;

4. The Director assessed an additional $1,291.85 for 1972 on account of a federal income tax adjustment. Taxpayer has not contested this adjustment.

(b) including one or more of the factors, such as expenses, purchases, contract values (minus subcontract values);

(c) excluding one or more assets in computing entire net worth;

(d) excluding one or more assets in computing an allocation percentage; or

(e) applying another similar or different method calculated to effect a fair and proper allocation of the entire net income and entire net worth reasonably attributable to the state.

Director denied the petition for the following reasons:

It is the Division's long standing position that § 8 does not authorize the Division to permit a taxpayer to report its net worth or net income tax on the basis of separate accounting, i.e., by including in the tax base only the assets and income centered or generated in New Jersey, to the exclusion of the assets and income generated elsewhere.

This position is based upon the fact that the statute, by its express terms, does not permit separate accounting and that the statute should not be circumvented to allow separate accounting by means of a § 8 judgment.

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It is also the Division's long standing position that § 8 does not permit a taxpayer to deduct encumbrances from the numerator or denominator of the property fraction. The deduction of such encumbrances is specifically prohibited by *N.J.A.C.* 18:7-8.5 and § 8 should not be read to circumvent this regulation.

In the present case, line 2(b) of schedule K of the taxpayer's CBT return shows that the taxpayer made sales to New Jersey customers. Thus, the taxpayer has not shown that each aspect of its business is entirely separate from every other aspect and that the statutory three-factor apportionment, formula produces an inequitable result.

In the present case, because the taxpayer's business is not segregated into distinct parts the taxpayer may not, by means of a § 8 adjustment, exclude investment income and investment securities from the net income and net worth basis respectively.[5]

The record shows that in denying taxpayer's petition Director reviewed no bookkeeping or accounting records of the corporation to determine if, in fact, the allocation formula was unfair or unreasonable. Instead he reviewed only the tax returns and subsequent correspondence between the parties. This appears to be an insufficient basis for the denial.

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5. These reasons were contained in the affidavit of the supervising auditor of the Division of Taxation.

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The additional assessments levied by Director resulted from an increase made by Director to taxpayer's net worth and net income. The increase in taxpayer's net income base was the result of combining income from manufacturing sales and securities investmens with its income from real estate holdings. Director used the company's net income (as reported for federal income tax purposes) and the New Jersey CBT which had been deducted for federal income tax purposes and then subtracted 50% of dividends received in accordance with *N.J.S.A.* 54:10A-4(k)(1). Taxpayer's New Jersey (pre-apportionment) income was then reflected as follows:

1971	1972	1973	1974
$767,543.92	$1,070,251.92	$1,347,059.36	$103,359.85

Director also changed taxpayer's net worth computations to correct, what he viewed as, a failure by taxpayer to adjust its investment securities to reflect their market value, as follows:

1971	1972	1973	1974
$267,309.59	$814,134.23	$990,057.80	($314,789.56)

After applying the apportionment fraction to these totals, taxpayer's adjusted net income, according to Director, resulted in apportioned net income of:

1971	1972	1973	1974
$222,770.41	$334,897.88	$355,311.15	$27,180.23

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Taxpayer contends that Director's mechanical use of the statutory method of allocation distorts its income attributable to New Jersey since management production, control and office location were centered in New York and that profits of the corporation for 1971 throught 1974 were completely generated by the manufacturing business in New York. In support of this argument it presented testimony and evidence that the company did not advertise in New Jersey magazines or newpapers, had a telephone listing only in the New York directory, that all orders were accepted at its New York factory as a result of customer-initiated inquiries, that it had no office or other facilities in New Jersey, had no employees or payroll allocable to New Jersey, that finished products were made available at the factory only, that it made no installations or deliveries in New Jersey and that there was no marketing effort directed toward New Jersey. Furthermore, no securities investments were held in New Jersey and the sole common denominator of the three aspects of the business was common ownership. This single feature, it argued, is insufficient to categorize the business as "unitary".

Director's claim that the manufacturing business and securities investments are linked together with the real estate operation in a manner sufficient to classify taxpayer as a "unitary" enterprise is founded, in part, on taxpayer's New Jersey sales tax returns.[6] Director asserts that sales of machinery by taxpayer to points within New Jersey and the subsequent collection of sales tax for these contracts constituted "doing business" in New Jersey.

6. Taxpayer asserted that its inclusion of the sales to New Jersey customers on Schedule K of the CBT was an error made in ignorance. It pointed out that it consistently presented the objection to apportionment of income from its manufacturing business and securities in its (1) tax return; (2) correspondence with the tax auditors; (3) in petition for administrative adjustment; and (4) in the pretrial order entered in the instant case.

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Director points out that reported sales in New Jersey by taxpayer were $436,566 in 1971, $986,862 in 1972, $998,740 in 1973 and $706,410 in 1974.

Director's arguments however fail to recognize the deceptive nature of these gross sales in light of the cost of the machinery which was sold, which cost ranged from $50,000 to $200,000 per machine. When these costs are compared to the total sales figures, one is not given the impression that sales of any great magnitude were made in New Jersey.

Taxpayer is correct in its assertion that, although a company's unrelated presence within a state may provide a sufficient jurisdictional basis to support liability for collection of a state's indirect sales tax, this presence is not sufficient to justify collection of franchise taxes which constitute a direct charge on interstate commerce. *See National Geographic Society v. California Board of Equalization,* 430 *U.S.* 551, (1977) (solicitation of mail orders for acceptance out-of-state did not constitute "doing business" so as to subject the company to state franchise tax; mere solicitation without a substantial related presence within the taxing state cannot constitutionally support the imposition of a direct tax, such as the franchise tax). The lack of a rational relationship between taxpayer's presence in New Jersey (real estate operation) and the specific business aspect (the manufacturing operations) which the state seeks to include within the franchise tax precludes the taxation of income derived from the latter activity.

The court further finds no rational relationship or nexus between taxpayer's securities portfolio and its presence in New Jersey. The question of whether a state may apportion income from a foreign corporation's intangible assets was addressed in

ASARCO, supra, at 801-804. ASARCO, a metal refining firm domiciled in New York, was taxed by Idaho on the revenues it received from a silver mine it operated in Idaho, and on dividend and interest income the company received from its security holdings in domestic and foreign corporations involved in other areas of the metal refining industry. The court found that although there were similarities between ASARCO and the companies in which it held securities, a full analysis of the "underlying economic realities" revealed that the security holdings were a "discrete business activity" which was disassociated with, and unrelated to, its presence in Idaho. *Id.* at 802. The court reiterated the warning against taxation on investment income given in *Mobil Oil Corp. v. Commissioner of Taxes of Vermont,* 445 *U.S.* 425 (1980) that:

> . . . We caution that we did not mean to suggest that all underlying dividend income received by corporations operating in interstate commerce is necessarily taxable in each state where that corporation does business. Where the business activities of the dividend payor have *nothing to do* with the activities of the recipient in the taxing state, *due process considerations might well preclude apportionability,* because there would be no underlying unitary business. *ASARCO, supra,* 50 *L.W.* at 4965 quoting *Mobil, supra,* 445 *U.S.* at 441-442, 100 S. Ct. at 1233-1234 [emphasis original].

As evidenced at trial, taxpayer's security holdings resembled those of an institutional investor. Director argues that the securities were purchased in order to acquire vertical and horizontal control

of the machine industry and points to taxpayer's majority holdings in four companies which he views as "potential" suppliers for taxpayer's hoist business. This argument fails for two reasons. First, in *ASARCO* and *Woolworth* it was held that possession of a majority interest which provided a bare "potential" for control does not establish sufficient criterion to justify characterization of a business as "unitary". It was stated:

> Our decision in *ASARCO* makes clear, however, that the *potential* to operate a company as part of a unitary business is not dispositive when, looking at "the 'underlying economic realities of a unitary business,' " the dividend income from the subsidiaries *in fact* is "derive[d] from 'unrelated business activity' which constitutes a 'discrete business enterprise.' " *Woolworth*, 50 *L.W.*, at 4959 [emphasis original].

Secondly, even if the evidence had demonstrated an attempt by taxpayer to gain control of the machinery business, such proof would have only served to establish "a relationship of sorts" between the manufacturing business and the securities investment operation and not with the real estate operation in New Jersey.

In a further attempt to show taxpayer to be a "unitary" business Director classified the company's operation as one of a centralized nature claiming that the job responsibilities of the chief operating officer, the company's single set of accounts, its bank accounts and its tax reporting on a unitary basis for purposes of New York taxation were indicia of centralized management, one of the three factors indicative of a unitary enterprise. These contentions are unconvincing so as to mandate taxation of taxpayer

as a unitary business. The position of chief officer does not serve as a boiler plate classification so as to equate the right of oversight to the scheme of exclusive and centralized management. In fact, the corporate structure envisions the overseeing of the business by directors and/or chief officers. Evidence was introduced by taxpayer, and uncontroverted by Director, that the operational management of the three businesses was actually diffused among several individuals. The facts reflect that centralized ownership and not centralized management is a proper adjective to describe the personality of the corporation.

The notion that a corporation's accounting system is an evidentiary tool to prove or disprove the unitarian nature of its business has been rejected by the court in *Mobil* and *Exxon*. The ease with which accounting records may be structured in order to reflect a desired image of the company's business makes it an unreliable factor by which to demonstrate the economic realities of an operation. *See* generally *Hallerstein, Recent Developments in State Tax Apportionments and The Circumscription of Unitary Business,* 21 *Nat'l. Tax J.* 487, 502-503 (1968) cited in *Mobil, supra,* 445 U.S. at 439. Most recently in *ASARCO* and *Woolworth,* attempts to classify diversified businesses as unitary by presenting evidence of centralized accounting, record keeping, consolidated annual reports and federal income tax preparation were rejected.

Director's reliance on taxpayer's method of New York tax computation is misplaced. New York is taxpayer's state of domicile. Its tax reporting method differs from that required by New Jersey. New York taxes and the computation of such are irrelevant.

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Similarly, Director's arguments that taxpayer's deposits in a single bank account of monies derived from all three businesses does not indicate a unitary enterprise. This concept was expressly rejected in *ASARCO* and *Woolworth.* In *ASARCO* it was held that although investment income from securities generally contributed to the corporation's overall wealth and strengthened the corporation's business, it was not a substitute for an actual unitary enterprise.

> Idaho's (taxing state) proposal is that a corporate purpose should define unitary business . . . This definition of a unitary business would destroy the concept. The business of a corporation requires that it earn money to continue operation and to provide return on its invested capital. Consequently *all* of its operations, including any investment made, in some sense can be said to be for "purposes related to or contributing to (corporation's) business." When pressed to its logical limit, this conception of the "unitary" business limitation becomes no limitation at all. When less ambitious interpretations are employed, the result is simply arbitrary. 73 *L.Ed.*2d at 801.

Likewise in *Woolworth,* it was held that the potential use of an unrelated business for financial collateral and the consequent commingling of profits from that unrelated business in a single operating fund was insufficient rationale to find the company unitary.

> . . . As relevant here, "the income attributed to a state for tax purposes" must be rationally related

> to values connected with the state. [citations omitted]. The state court's reasoning would trivialize this due process limitation by holding it is satisfied that the income in question "adds to the riches of the corporation. . . ." [citations omitted]. Income, from whatever source, always is a "business advantage" to a corporation. Our cases demand more. In particular, they specify that the proper inquiry looks to the "underlying unity or diversity of business enterprise", . . not to whether the non-domiciliary parent derives some economic benefit—as it firstly always will—from its ownership of stock in another corporation. *Woolworth,* 73 *L.Ed.*2d. 827.

It is the opinion of the court that taxpayer is a non-unitary corporation which, except for its New Jersey real estate holdings, cannot be held subject to apportionment or taxation for CBT purposes. The underlying economic realities of the corporation lead me to conclude that taxpayer's business consists of three distinct operations; manufacturing, real estate and securities investments. The necessary relationship "to opportunities, benefits, or protection conferred or afforded by the taxing state", do not here exist so as to warrant the deficiency assessments levied by Director. *See Wisconsin v. J.C. Penney Co.,* 311 *U.S.* 435, 444 (1940).

The Clerk of the Tax Court is directed to enter judgment in favor of taxpayer.

APPENDIX C—DECISION OF THE SUPERIOR COURT OF NEW JERSEY, APPELLATE DIVISION

SUPERIOR COURT OF NEW JERSEY
APPELLATE DIVISION

A-3554-82T2

SILENT HOIST & CRANE CO., INC.,

Plaintiff-Respondent,

v.

DIRECTOR, DIVISION OF TAXATION,

Defendant-Appellant.

Argued: March 19, 1984—Decided: April 4, 1984

Before Judges Bischoff, Petrella and Brody.

On appeal from The Tax Court of New Jersey.

Mary R. Hamill, Deputy Attorney General, argued the cause for appellant (Irwin I. Kimmelman, Attorney General of New Jersey, attorney; James J. Ciancia, Assistant Attorney General, of counsel).

Daniel E. Horgan argued the cause for respondent (Waters, McPherson, McNeill, P.A., attorneys).

Appendix C

PER CURIAM

The Director, Division of Taxation appeals the determinations of the Tax Court which held in favor of the taxpayer as to the nonapplicability of the New Jersey Corporation Business Tax (*N.J.S.A.* 54:10A-1, *et seq.*).

We affirm substantially for the reasons expressed in Judge Evers' opinion reported at 5 *N.J.Tax* 242 (Tax Ct. 1983).

A True Copy

Elizabeth McLaughlin, Clerk

APPENDIX D—RELEVANT STATUTES

The New Jersey Corporation Business Act, *N.J.S.A.* 54:10A provides in pertinent part:

> **54:10A-6. Taxpayer maintaining regular place of business outside state**
>
> In the case of a taxpayer which maintains a regular place of business outside this State other than a statutory office, the portion of its entire net worth to be used as a measure of the tax imposed by section 5(a) of this act,[1] and the portion of its entire net income to be used as a measure of the tax imposed by section 5(c) of this act, shall be determined by multiplying such entire net worth and entire net income, respectively, by an allocation factor which shall be the average of the fractions computed in (A), (B) and (C) below, or of so many of them as may be applicable, that is:
>
> (A) The average value of the taxpayer's real and tangible personal property within the State during the period covered by its report divided by the average value of all the taxpayer's real and tangible personal property wherever situated during such period; provided, however, that for the purpose of determining average value, the provisions with respect to depreciation as set forth in paragraph 2(F) of subsection (k) of section 4 of P.L.1945, c. 162 (C. 54:10A-4) shall be taken into account for arriving at such value.
>
> (B) The receipts of the taxpayer, computed on the cash or accrual basis according to the

method of accounting used in the computation of its net income for federal tax purposes, arising during such period from

(1) sales of its tangible personal property located within this State at the time of the receipt of or appropriation to the orders where shipments are made to points within this State,

(2) sales of tangible personal property located without the State at the time of the receipt of or appropriation to the orders where shipment is made to points within the State,

(3) (Deleted by amendment.)

(4) services performed within the State,

(5) rentals from property situated, and royalties from the use of patents or copyrights, within the State,

(6) all other business receipts (excluding dividends excluded from entire net income by subsection (k)(1) of section 4 hereof)[2] earned within the State, divided by the total amount of the taxpayer's receipts, similarly computed, arising during such period from all sales of its tangible personal property, services, rentals, royalties and all other business receipts, whether within or without the State;

Appendix D

For the purposes of this section, receipts shall not include any sum or sums of money received in payment for gas or electric energy sold to a public utility subject to taxation pursuant to P.L.1940, c. 5 (C. 54:30A-49 et seq.) for resale to ratepayers of the public utility.

(C) The total wages, salaries and other personal service compensation, similarly computed, during such period of officers and employees within the State divided by the total wages, salaries and other personal service compensation, similarly computed, during such period of all the taxpayer's officers and employees within and without the State.

In the case of a taxpayer which does not maintain a regular place of business outside this State other than a statutory office, the allocation factor shall be 100%.

* * * * *

54:10A-8. Adjustment of allocation factor

If it shall appear to the commissioner that an allocation factor determined pursuant to section 6[1] does not properly reflect the activity, business, receipts, capital, entire net worth or entire net income of a taxpayer reasonably attributable to the State, he may adjust it by:

(a) excluding one or more of the factors therein;

(b) including one or more other factors, such as expenses, purchases, contract values (minus subcontract values);

(c) excluding one or more assets in computing entire net worth; or

(d) excluding one or more assets in computing an allocation percentage; or

(e) applying any other similar or different method calculated to effect a fair and proper allocation of the entire net income and the entire net worth reasonably attributable to the State.

* * * * *